

UNEMPLOYMENT INSURANCE FUND  
SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION

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FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT  
JUNE 30, 2011

# **SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

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# Ketel Thorstenson, LLP

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## INDEPENDENT AUDITOR'S REPORT

The Honorable Dennis Daugaard  
Governor of South Dakota  
and  
The South Dakota Department of Labor and Regulation

We have audited the accompanying financial statements of the **UNEMPLOYMENT INSURANCE FUND OF THE SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION** (the Fund) as of and for the year ended June 30, 2011, as detailed in the table of contents. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Unemployment Insurance Fund and do not purport to, and do not, present fairly the financial position of the South Dakota Department of Labor and Regulation or the State of South Dakota, as of June 30, 2011, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the **UNEMPLOYMENT INSURANCE FUND OF THE SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION** as of June 30, 2011, and the results of its operations and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued a report dated December 6, 2011, on our consideration of the Fund's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

The Honorable Dennis Daugaard  
Governor of South Dakota  
and  
The South Dakota Department of Labor and Regulation

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Our audit was performed for the purpose of forming an opinion on the financial statements as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," and is not a required part of the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

A handwritten signature in black ink that reads "Ketel Thorstenson, LLP". The signature is written in a cursive, flowing style.

KETEL THORSTENSON, LLP  
Certified Public Accountants

December 6, 2011

**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**BALANCE SHEET**

**UNEMPLOYMENT INSURANCE FUND**

**JUNE 30, 2011**

**Assets**

**Current Assets**

Cash (Note 2)	\$ 28,409,935
Receivables, Net of Allowance for Doubtful Accounts of \$3,085,387	2,009,148
Receivable From Other Governments	480,554
Receivable From Other State Funds (Note 3)	89,491
<b>Total Assets</b>	<b>\$ 30,989,128</b>

**Liabilities and Net Assets**

**Current Liabilities**

Payable to Futures Fund	\$ 8,031
Payable to Fiscal Administration Fund	543,693
Payable to Employment Security Contingency Fund	293,861
<b>Total Current Liabilities</b>	<b>845,585</b>

**Commitments (Note 4)**

**Net Assets**

Unrestricted	30,143,543
<b>Total Liabilities and Net Assets</b>	<b>\$ 30,989,128</b>

The accompanying notes are an integral part of this statement.

**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS  
UNEMPLOYMENT INSURANCE FUND  
FOR THE YEAR ENDED JUNE 30, 2011**

<b>Operating Revenues</b>	
Taxes	\$ 74,452,973
<b>Operating Expenses</b>	
Unemployment Insurance Benefits	63,618,471
<b>Operating Income</b>	<b>10,834,502</b>
<b>Non-Operating Revenue</b>	
Revenue From the Use of Money	2,303,550
<b>Transfers</b>	
Transfers To Other State Funds	(1,432,707)
Transfers From Other State Funds	623,078
<b>Total Transfers</b>	<b>(809,629)</b>
<b>Change in Net Assets</b>	<b>12,328,423</b>
<b>Total Net Assets -- June 30, 2010</b>	<b>17,815,120</b>
<b>Total Net Assets -- June 30, 2011</b>	<b>\$ 30,143,543</b>

The accompanying notes are an integral part of this statement.

**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**STATEMENT OF CASH FLOWS  
UNEMPLOYMENT INSURANCE FUND  
FOR THE YEAR ENDED JUNE 30, 2011**

<b>Cash Flows From Operating Activities</b>	
Receipts from Employers	\$ 74,401,803
Payments for Benefits	(63,618,471)
Net Receipts from Other Funds	103,448
<b>Net Cash Flows Provided by Operating Activities</b>	<b>10,886,780</b>
<b>Cash Flows From Non-Capital Financing Activities</b>	
Transfer To Employment Security Contingency Fund	(1,432,707)
Transfer From Employment Security Contingency Fund	623,078
<b>Net Cash Flows Used in Non-Capital Financing Activities</b>	<b>(809,629)</b>
<b>Cash Flows From Investing Activities</b>	
Pooled Investment Income	2,303,550
<b>Net Increase in Cash During the Year</b>	<b>12,380,701</b>
<b>Cash – Beginning of Year</b>	<b>16,029,234</b>
<b>Cash – End of Year</b>	<b>\$ 28,409,935</b>
<b>Reconciliation of Operating Income to Net Cash Flows Provided by Operating Activities:</b>	
Operating Income	\$ 10,834,502
Increase in Receivables	(51,170)
Decrease in Receivable From Other Governments	140,622
Decrease in Receivable From Other State Funds	29,508
Decrease in Payable to Other State Funds	(66,682)
<b>Net Cash Flows Provided by Operating Activities</b>	<b>\$ 10,886,780</b>

The accompanying notes are an integral part of this statement.

## **SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

### **NOTES TO THE FINANCIAL STATEMENTS UNEMPLOYMENT INSURANCE FUND JUNE 30, 2011**

#### **(1) Summary of Significant Accounting Policies**

##### **a. Reporting Entity**

The South Dakota Department of Labor and Regulation (the Department) is the state agency responsible for providing job placement services, job training services, unemployment insurance services, and the enforcement of state labor laws. The Unemployment Insurance Fund (the Fund) is used to account for tax receipts from employers within the State of South Dakota and to account for benefits paid to unemployed persons. The accompanying financial statements present only the financial condition and results of operations of the Fund and do not represent a complete presentation of the Department's net assets and activities.

##### **b. Fund Accounting**

The accounts of the Unemployment Insurance Fund are organized for accounting and reporting purposes on the basis of fund accounting. The operations of the Fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, net assets, revenues, and expenses.

##### ***Proprietary Funds:***

Enterprise Fund - enterprise funds are used to report a governmental activity funded by a charge to external users of services.

The Fund does not apply any FASB Statements and Interpretations issued after November 30, 1989.

Unemployment Insurance Fund - an enterprise fund established to account for funds that are expended for benefits paid to unemployed South Dakota workers. Fund revenues are collected from South Dakota employers based upon a percentage of qualifying wages paid, and from direct federal funding. Cash balances of the Unemployment Insurance Fund are required to be deposited with the U.S. Department of Treasury.

##### **c. Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates. Significant estimates not disclosed elsewhere in the accompanying financial statements include:

An allowance for uncollectible receivables is maintained at a level which management believes is adequate to absorb probable uncollectible accounts. Management determines the adequacy of the allowance based on historical data, current economic conditions, and other pertinent factors for the Fund.

It is reasonably possible that this estimate will change significantly in the near term.

##### **d. Basis of Accounting**

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements.

Proprietary funds are accounted for using the accrual basis of accounting. Revenues from unemployment taxes collected from employers are recognized in the period received because the amounts cannot be reasonably estimated prior to collection. Expenditures are generally recognized when the related fund liability is incurred.



**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**UNEMPLOYMENT INSURANCE FUND**  
**JUNE 30, 2011**

**(1) Summary of Significant Accounting Policies (Continued)**

**e. Proprietary Funds Revenue and Expense Classifications**

In the proprietary fund's Statement of Revenues, Expenses, and Changes in Fund Net Assets, revenue and expenses are classified in a manner consistent with how they are classified in the Statement of Cash Flows. That is, transactions for which related cash flows are reported as capital and related financing activities, noncapital financing activities, or investing activities are not reported as components of operating revenues or expenses.

**(2) Cash**

Various restrictions on deposits and investments are imposed by statutes. These restrictions are summarized below:

**Deposits** – The Department's deposits are made in qualified public depositories as defined by SDCL 4-6A-1, 13-16-15, 13-16-15.1, and 13-16-18.1. Qualified depositories are required by SDCL 4-6A-3 to maintain at all times, segregated from their other assets, eligible collateral having a value equal to at least 100 percent of the public deposit accounts that exceed deposit insurance such as the FDIC and NCUA. In lieu of pledging eligible securities, a qualified public depository may furnish irrevocable standby letters of credit issued by federal home loan banks accompanied by written evidence of the bank's public debt rating, which may not be less than "AA" or better, or a qualified public depository may furnish a corporate surety bond of a corporation authorized to do business in South Dakota.

**Investments** – In general, SDCL 4-5-6 permits funds to be invested only in (a) securities of the United States and securities guaranteed by the United States Government either directly or indirectly; or (b) repurchase agreements fully collateralized by securities described in (a) above; or in shares of an open-end, no-load fund administered by an investment company whose investments are in securities described in (a) above and repurchase agreements described in (b) above. Also, SDCL 4-5-9 requires investments to be in the physical custody of the political subdivisions or may be deposited in a safekeeping account with any bank or trust company designated by the political subdivision as its fiscal agent.

As of June 30, 2011, the Fund's cash consisted only of checking and pooled US Treasury Unemployment Insurance Funds. All of these accounts are insured or collateralized in the Fund's name. The Fund has no investment policies to restrict its investments beyond the state requirements noted above.

**Custodial Credit Risk** – The risk that, in the event of a depository failure, the Fund's deposits may not be returned to it. The Fund does not have a deposit policy for custodial credit risk. As of June 30, 2011, none of the Fund's deposits were exposed to custodial credit risk.

**(3) Receivable from Other State Funds**

The receivable from other state funds relates to unemployment insurance benefits paid to employees of other state agencies.

**(4) Commitments**

Benefit payments to unemployed persons (claimants) are recorded when paid. Unemployed persons may receive benefit payments for up to the lesser of twenty-six payments at their maximum weekly amounts (may be extended as part of the ongoing federal programs currently in place) or as long as they continue to be eligible to receive payments. Eligibility to continue to receive benefit payments is determined on a weekly basis. Accordingly, no liability has been recorded for future benefit payments. The maximum remaining amount of benefits payable to unemployed persons at June 30, 2011, is not determinable; however, the amount would be significant to the Fund's financial statements.

## SUPPLEMENTARY INFORMATION

**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
UNEMPLOYMENT INSURANCE FUND  
FOR THE YEAR ENDED JUNE 30, 2011**

<b>FUNDING SOURCE PROGRAM NAME</b>		<b>FEDERAL CFDA NUMBER</b>	<b>FEDERAL EXPENDITURES</b>
<b>U.S. Department of Labor</b>			
Direct Programs:			
State Unemployment Insurance Benefits (Note 1)	*	17.225	\$ 42,609,578
Federal Unemployment Insurance Benefits	*	17.225	9,094,044
ARRA - Federal Additional Compensation Unemployment Insurance Benefits	*	17.225	1,594,180
ARRA - Federal Emergency Unemployment Insurance Benefits	*	17.225	10,320,669
<b>Total Federal Funds Expenditures</b>			<b>\$ 63,618,471</b>

Note 1 - This amount represents the State's expenditures for unemployment benefits and is reported as a major federal program as required by the U.S. Department of Labor and Regulation and the Inspector General. Included in this balance is \$9,769,534 of state unemployment benefits that were paid with funds from the Federal Unemployment Compensation Modernization Program (ARRA).

\* Considered major federal assistance programs pursuant to Department of Legislative Audit requirements.

This schedule is prepared on the accrual basis of accounting.

## OTHER REPORTS



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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND  
ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL  
STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To Honorable Dennis Daugaard  
Governor of South Dakota  
and  
The South Dakota Department of Labor and Regulation

We have audited the financial statements of the **UNEMPLOYMENT INSURANCE FUND OF THE SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION** (the Fund) as of and for the year ended June 30, 2011, and have issued our report thereon dated December 6, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

## **Internal Control over Financial Reporting**

In planning and performing our audit, we considered the Fund's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and another deficiency that we consider to be a significant deficiency.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Fund's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs in Part B Findings #2011-1 and 2011-2 to be material weaknesses.

A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying Schedule of Findings and Questioned Costs in Part B Finding #2011-3 to be a significant deficiency.

To Honorable Dennis Daugaard  
Governor of South Dakota  
and  
The South Dakota Department of Labor and Regulation

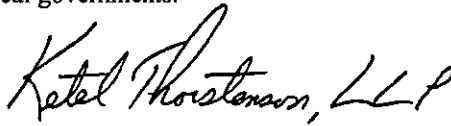
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### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

The Fund's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the Fund's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the State of South Dakota's management, federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than those specified parties. However, as required by South Dakota Codified Law 4-11-1, this report is a matter of public record and its distribution is not limited for state and local governments.



KETEL THORSTENSON, LLP  
Certified Public Accountants

December 6, 2011



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**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS  
THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND  
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

To Honorable Dennis Daugaard  
Governor of South Dakota  
and  
The South Dakota Department of Labor and Regulation

## **Compliance**

We have audited the compliance of the **UNEMPLOYMENT INSURANCE FUND OF THE SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION** (the Fund) with the types of compliance requirements described in the "U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement" that could have a direct and material effect on its major federal program for the year ended June 30, 2011. The Fund's major federal program is identified in the summary of audit results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of the Fund's management. Our responsibility is to express an opinion on the Fund's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations." Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Fund's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Fund's compliance with those requirements.

In our opinion, the Fund complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2011. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs Part C Findings #2011-4, 2011-5 and 2011-6.

## **Internal Control over Compliance**

Management of the Fund is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Fund's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control over compliance.

To Honorable Dennis Daugaard  
Governor of South Dakota  
and  
The South Dakota Department of Labor and Regulation

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Our consideration of the internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in the internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs in Part B Finding #2011-2 and Part C Finding #2011-4 to be material weaknesses.

A significant deficiency in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as Part C Findings #2011-5 and 2011-6 to be significant deficiencies.

The Fund's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the Fund's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the State of South Dakota's management, federal awarding agencies and pass-through entities and is not intended to be, and should not be used by anyone other than those specified parties. However, as required by South Dakota Codified Law 4-11-1, this report is a matter of public record and its distribution is not limited for state and local governments.



KETEL THORSTENSON, LLP  
Certified Public Accountants

December 6, 2011



**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
UNEMPLOYMENT INSURANCE FUND  
FOR THE YEAR ENDED JUNE 30, 2011**

**A. Summary of Audit Results**

1. The independent auditor's report expresses an unqualified opinion on the financial statements of the Unemployment Insurance Fund (the Fund).
2. Three deficiencies relating to the audit of the financial statements are reported in the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards. Two deficiencies were considered to be material weaknesses.
3. No instances of noncompliance material to the financial statements of the Fund were disclosed during the audit.
4. Four deficiencies relating to the audit of the major federal award program are reported in the Independent Auditor's Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133. Two deficiencies were considered to be material weaknesses.
5. The independent auditor's report on compliance for the major federal award program for the Fund expresses an unqualified opinion.
6. Audit findings relative to the major federal award program are reported in Part C of this schedule.
7. The program tested as a major program included: State and Federal Unemployment Insurance CFDA# 17.225.
8. The threshold used for distinguishing between Type A and B programs was \$7,300,000.
9. The Department was not considered a low risk auditee under the criteria established in OMB Circular A-133.

**B. Findings -- Financial Statement Audit**

***Material Weaknesses***

**2011-1: Audit Adjustments**

*Condition:* During the course of our audit engagement, we proposed material audit adjustments that resulted in significant changes in the Fund's financial statements. Adjustments included recording federal benefit payments, adjusting the allowance for doubtful accounts, adjusting the fiscal administration liability, recording the amount due to contingency fund and correcting the netting of transfers to/from contingency fund, and recording the amount due to futures fund. These adjustments were not identified as a result of the Fund's existing internal controls, and therefore, could have resulted in a material misstatement of the Fund's financial statements.

*Cause:* The Fund relies on the auditor to record necessary entries to convert their cash basis trial balance to accrual basis and to record the federal benefit payments.

*Criteria and Effect:* It is the responsibility of management to implement and operate effective internal controls to identify and detect potentially material adjustments to the financial records.

**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
UNEMPLOYMENT INSURANCE FUND  
FOR THE YEAR ENDED JUNE 30, 2011**

**B. Findings -- Financial Statement Audit (Continued)**

*Material Weaknesses (Continued)*

2011-1: Audit Adjustments (Continued)

*Recommendations:* Accounting staff should ensure all necessary adjustments have been posted to provide the auditors with an accrual basis trial balance. Normal year-end adjustments should be made by accounting staff of the Fund. In addition, we recommend changes in operations be continually reviewed for potential changes in accounting so that the appropriate entries can be made throughout the year. We believe the Senior Accountant has the competency and ability to make the necessary adjustments to convert the cash basis accounting system to accrual basis in preparation for the audit.

*Response/Corrective Action Plan:* During the next fiscal year, we will continue to utilize the senior internal auditor from the Department of Labor and Regulation, Unemployment Insurance Division to review our financial statements on a quarterly basis and adjustments to accounts made as needed. In addition to making timely adjustments to accounts, the senior accountant will provide to the auditors the adjusted amounts needed for the financial statements for FY12. A formal policy will be written to put this into place. The Deputy UI Director will be in charge of implementation of the corrective action plan.

2011-2: Preparation of the Financial Statements

*Condition:* We were requested to draft the audited financial statements, related footnote disclosures and Schedule of Expenditures of Federal Awards as part of our regular audit services. Ultimately, it is management's responsibility to provide for the preparation of the Fund's financial statements, related footnote disclosures and Schedule of Expenditures of Federal Awards, and the responsibility of the auditor to determine the fairness of presentation of those financial statements, footnotes and supporting schedule. From a practical standpoint, we do both for the Fund at the same time in connection with our audit.

*Cause:* The Fund does not employ an individual with qualifications necessary to ensure the financial statements, related footnote disclosures, and Schedule of Expenditures of Federal Awards meet generally accepted accounting principles.

*Criteria and Effect:* It is our responsibility to inform the Fund's management and those charged with governance that this deficiency could result in a misstatement to the financial statements that could have been prevented or detected by the Fund's management.

*Recommendation:* As in prior years, we have instructed management to review a draft of the auditor prepared financials in detail for their accuracy; we have answered any questions they might have, and have encouraged research of any accounting guidance in connection with the adequacy and appropriateness of classification and disclosure in your statements. We are satisfied that the appropriate steps have been taken to provide the Fund with the completed financial statements. It is the responsibility of the Fund's management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
UNEMPLOYMENT INSURANCE FUND  
FOR THE YEAR ENDED JUNE 30, 2011**

**B. Findings -- Financial Statement Audit (Concluded)**

***Material Weaknesses (Continued)***

**2011-2: Preparation of the Financial Statements**

*Response/Corrective Action Plan:* We are aware of the risk associated with not preparing our financial statements, but believe our review of the financial statements to be adequate to reduce the risk. The financial statements are viewed by management and accounting staff of the South Dakota Department of Labor and Regulation, Division of Administrative Services and accounting staff of the Division of Unemployment Insurance. Administration review includes, but is not limited to, assurances that certain financial statement entries are accurately reported. This is imperative because corresponding entries are posted to the State's Comprehensive Annual Financial Report. The South Dakota Bureau of Finance and Management also review the completed financial statements to ensure corresponding entries are accurate.

***Significant Deficiency***

**2011-3: Review of Journal Entry Postings**

*Condition:* During the year, the Fund implemented a new quarterly review process over the general ledger balances; however, the review process does not include a review of adjusting entries posted.

*Cause:* The quarterly review process does not include a review of the adjusting entries posted.

*Criteria and Effect:* It is the responsibility of management to implement and operate effective internal controls over adjusting entries. An appropriate level of review ensures financial records are accurate.

*Recommendation:* The quarterly review of the general ledger balances by the Senior Auditor should include a review of all adjusting entries posted.

*Response/Corrective Action Plan:* In addition to implementing changes to the policy for the quarterly review of the general ledger balances this past year, we recently added a review and confirmation of the adjustments resulting from the review to the policy. The Deputy UI Director remains in charge of implementation of the corrective action plan.

**C. Findings and Questioned Costs -- Major Federal Award Programs Audit**

Finding #2011-2 in Part B above relates to the Fund's major federal program.

***Material Weakness***

**2011-4: EUC Benefit Payment**

*Condition:* During our testing of Emergency Unemployment Compensation (EUC) benefit payments, we noted four errors in the EUC calculations. One error was due to the Fund using the maximum unemployment benefit amount instead of the claimant's maximum regular unemployment benefit amount as a basis for calculating the maximum Tier I EUC benefit amount. Three errors were due to the Fund using the maximum Tier I EUC benefit amount as a basis for calculating the maximum EUC Tier II benefit amount instead of the maximum regular unemployment benefit amount.

**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
UNEMPLOYMENT INSURANCE FUND  
FOR THE YEAR ENDED JUNE 30, 2011**

**C. Findings and Questioned Costs -- Major Federal Award Programs Audit (Continued)**

***Material Weakness (Continued)***

**2011-4: EUC Benefit Payment (Continued)**

*Cause:* The EUC benefits are the result of a temporary federal program and therefore are unusual to the Fund's normal benefit payment processing. The Fund lacks a review process of the manual calculation to determine the maximum EUC benefits for both Tiers.

*Criteria and Effect:* The EUC Tier I and Tier II maximum benefit amounts were to be calculated using the maximum regular unemployment benefit amount.

*Questioned Costs:* None – The Fund's correction of miscalculations of the maximum EUC benefit while the claimant's case is still active will prevent overspending of the claimant's maximum benefits allowed in the instances of the errors noted above.

*Recommendation:* We recommend the maximum EUC Tier I and Tier II benefit amount calculations be internally reviewed for accuracy by someone other than the individual performing the calculation and prior to the claimant's notice of benefits being generated.

*Response/Corrective Action Plan:* The requirements for EUC claim monetary determinations were reviewed with staff. A new procedure to verify the accuracy of the monetary determinations periodically will be added to the process. The Deputy UI Director will be in charge of implementation of the corrective action plan.

***Significant Deficiencies***

**2011-5: Mischarge to Employer Account**

*Condition:* During our testing of benefit payments, it was noted that one employer account was charged for benefit payments when the employer should have been relieved as a result of the claimant indicating they had voluntarily quit without good cause from this place of employment.

*Cause:* There was a lag in time from the point when the claimant filed to the point when benefits were paid due to a multi-state wage verification. Once the verification was received, there were multiple weeks of backpay issued to the claimant in one week. The backpay exceeded the liable employer's allocation of benefits and was then charged to the subsequent employer in the required inverse order. However, the notice of charges was not sent to the subsequent employer and its account was charged despite the claimant indicating he had quit this place of employment. The program is automated to send the notification to the employer and this error was the result of the automation not operating effectively.

*Criteria and Effect:* Per SDCL 61-5-29, no benefits paid on the basis of a period of employment may be charged to the experience-rating account of any employer, except as provided in SDCL 61-5-29.2, if the claimant voluntarily separated without good cause attributable to the employer or the employment. It is the responsibility of the Fund to ensure that benefit payments made are allowable.

*Questioned Costs:* None

*Recommendation:* We recommend an employer be provided the notice of charges and its account be relieved of charges of benefits when the claimant indicates he/she voluntarily separated without good cause.

**SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONCLUDED)  
UNEMPLOYMENT INSURANCE FUND  
FOR THE YEAR ENDED JUNE 30, 2011**

**C. Findings and Questioned Costs -- Major Federal Award Programs Audit (Concluded)**

***Significant Deficiencies (Continued)***

*Response/Corrective Action Plan:* Policy is to relieve employers when the claimant indicates he/she voluntarily separated without good cause. Computer automation is in place to ensure notices of claim are mailed to employers. However, in this instance, the programming may have failed due to the large number of weekly certifications paid at one time. Employees involved in this activity were instructed after the FY11 audit to limit the total number of weekly certifications processed for any one claimant during a check run. Also, employees involved in this activity were reminded of policy. The corrective action plan has already been implemented. The Deputy UI Director remains in charge of this corrective action plan.

**2011-6: Allowability of Benefit Payments**

*Condition:* We noted during testing that one benefit payment recipient applied for and received UCX payments though the claimant was discharged from the military under an "Other than Honorable Discharge."

*Cause:* The Fund's understanding was based on outdated guidance.

*Criteria and Effect:* Regulations governing UCX payments state claimants are only eligible if they have been discharged under "Honorable" conditions. Additionally, the Fund just recently received a letter of denial from the US Marines for these benefits paid.

*Questioned Costs:* None

*Recommendation:* We recommend the Fund ensure any ex-military claimant was not terminated from the service for "Other than Honorable Discharge" as such claimant is not eligible to be receiving benefits.

*Response/Corrective Action Plan:* This occurrence was the result of a misinterpretation of the documentation provided by the USDOL and the Department of Defense. Employees involved in this activity were instructed on the correct interpretation of the guidance. The Deputy UI Director remains in charge of the corrective action plan.

**Status of Prior Audit Findings**

Audit findings 2010-1, 2010-2, and 2010-5 for the year ending June 30, 2010 are repeated as findings 2011-1, 2011-2, and 2011-5, respectively, for the year ending June 30, 2011.

The Fund has implemented a quarterly review process over the general ledger balances. This process includes the review and resolution of bank reconciliation issues. At year-end of the current year, no bank reconciliation discrepancies were noted; however, we did note the general journal entries posted by the senior accountant are not being reviewed. Therefore, finding 2010-3 has been repeated in part as finding 2011-3, as noted above.

The Fund had reverted back to the old employer tax program and monthly processing was being performed timely beginning in December 2009. The transition to a new employer tax program had been the cause of the late filing of federal reports in the prior year. No federal reports were filed late as a result of this during the current year. Considering such, finding 2010-4 is not repeated in the current year.